

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

STATE OF SOUTH DAKOTA, EX REL.,

Petitioner,

v.

RICHARD B. OGILVIE, TRUSTEE OF THE PROPERTY
OF THE CHICAGO, MILWAUKEE, ST. PAUL AND
PACIFIC RAILROAD COMPANY,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

ROBERT H. WHEELER

(Counsel of Record)

LAWRENCE S. ADELSON

EDWARD W. MALSTROM

ISHAM, LINCOLN & BEALE

Three First National Plaza

Suite 5200

Chicago, Illinois 60602

(312) 558-7500

Counsel for Respondent

January 28, 1983

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REASONS FOR DENYING THE WRIT

1. The courts below applied law settled by this and other courts that setoffs are not allowed in Section 77 railroad reorganizations.

Paragraph 10 of Order No. 1 in the Milwaukee Road reorganization enjoins setoffs of obligations of the Debtor against claims against the Debtor. Such an order is typical in a railroad reorganization under Section 77.¹ See, e.g., *In re*

¹ 11 U.S.C. § 205 (repealed effective 1979) is referred to herein as Section 77. It continues to govern the Milwaukee Road reorganization. Pub. L. No. 95-598, § 403, 92 Stat. 2683 (1978).

Lehigh and Hudson River Ry. Co., 468 F.2d 430, 432 (2d Cir. 1962); *Penn Central Transp. Co. v. National City Bank*, 315 F.Supp. 1281, 1282 (E.D. Pa. 1970), 315 F.Supp. 1281 (E.D. Pa. 1970); *In re Chicago, Rock Island and Pacific R.R. Co.*, 537 F.2d 906, 913 (7th Cir. 1976), cert. denied, 429 U.S. 1092 (1977); *In re Central Railroad Co.*, 273 F.Supp. 282, 285 (D.N.J. 1967), aff'd 392 F.2d 589 (3d Cir. 1968).

This Court has stated that "[a]s a general rule of administration for Section 77 Reorganization Courts, setoff should not be allowed." *Baker v. Gold Seal Liquors*, 417 U.S. 467, 474 (1974). This rule has been consistently reiterated and followed by other federal courts faced with attempts to set off claims in Section 77 reorganizations.² See *In re Lehigh and Hudson, supra*, at 433; *Penn Central Transp. Co. v. National City Bank, supra*, at 1283-84; *In re Central R.R. Co., supra*.

The Seventh Circuit simply applied this rule to the case at hand. Petitioners have shown no uncertainty or disagreement in the courts regarding the rule and have made no case for its reconsideration.

2. The rationale of *Baker v. Gold Seal* applies to tax claims.

Petitioners argue that the rule against setoffs enunciated in *Baker v. Gold Seal* is limited to low-priority unsecured claims and does not apply to tax claims.

² The only exception has been in the specialized area of railroad interline per diem accounts governed by Interstate Commerce Commission regulations. The Seventh Circuit found that such accounts contain only net balances rather than offsetting claims. *In re Chicago, Rock Island and Pacific R.R. Co., supra*.

While *Baker* did involve low-priority unsecured claims, it sets forth a general rule which is not limited to those facts.³ The *Baker* Court enunciated two reasons for prohibiting setoffs in railroad reorganizations. Both aspects of the *Baker* rationale clearly apply, by logic and by precedent, to the tax claims at issue here. Therefore, there is no reason for this Court to consider this case. The first reason is the need to collect "amounts owed the bankrupt to keep its cash inflow sufficient for operating purposes, . . ." 417 U.S. at 471. It is clear that payment of taxes can be suspended to permit continuation of railroad operations. *In re Penn Central Transp. Co.*, 452 F.2d 1107 (3d Cir. 1971), cert. denied, 406 U.S. 944 (1972).

The second rationale is that "... to the extent that [a setoff] is allowed, it grants a preference to the claim of one creditor over the others . . . That is a form of discrimination to which the policy of § 77 is opposed." *Baker v. Gold Seal*, 417 U.S. at 474. This rationale applies with equal force to tax claims and freight claims. A setoff by a secured creditor wrongly prefers that creditor over other creditors, secured and unsecured, just as surely as a setoff by an unsecured creditor. In an analogous Section 77 case, where railroad property was condemned, the rule of *Baker* against discrimination was applied to prevent preferential payment of taxes out of the proceeds of the condemnation. *In re Penn Central Transp. Co.*, 383 F.Supp. 1128, 1130 (E.D. Pa. 1974).

³ The interests of high-priority, secured creditors can be suspended and altered in the interests of a successful reorganization. *New Haven Inclusion Cases*, 399 U.S. 392, 492 (1970); *Penn-Central Merger Cases*, 389 U.S. 486, 510-11 (1968). . .

CONCLUSION

Based upon the foregoing, Richard B. Ogilvie, Trustee of the Property of the Chicago, Milwaukee, St. Paul and Pacific Railroad Company prays that the Petitioner's Petition for a Writ of Certiorari be denied.

Respectfully submitted,

ROBERT H. WHEELER
LAWRENCE S. ADELSON
EDWARD W. MALSTROM
ISHAM, LINCOLN & BEALE
Three First National Plaza
Suite 5200
Chicago, Illinois 60602
(312) 558-7550

Counsel for Respondent

APPENDIX A
PARENT COMPANIES, SUBSIDIARIES
AND AFFILIATES

Richard B. Ogilvie as Trustee of the Property of the Chicago, Milwaukee, St. Paul & Pacific Railroad Company, Debtor, is the Respondent.

Prior to reorganization proceedings, the Chicago Milwaukee Corporation was the parent of the Debtor owning approximately 96% of its common and preferred stock. The Trustee is vested with title to the assets of the Milwaukee Road and is empowered to operate its business and otherwise deal with its assets and properties, subject to the jurisdiction of the Reorganization Court. It is the Trustee's opinion that Chicago Milwaukee Corporation and its subsidiaries are neither parent nor affiliates because the Property of the Milwaukee Road is controlled by the Trustee and the Reorganization Court rather than Chicago Milwaukee Corporation.

AFFILIATES

Chicago Union Station Company
Indiana Harbor Belt Railroad Company
Kansas City Terminal Railway Company
The Minnesota Transfer Railway Company
Minneapolis Eastern Railway Company
The Pullman Company
Trailer Train Company
Longview Switching Company
Northern Tier Pipeline Company

SUBSIDIARIES

Chicago, Terre Haute and Southeastern
Railroad Company
Davenport, Rock Island and North Western
Railway Company
DesMoines Union Railway Company
Milwaukee Land Company
The Milwaukee Motor Transportation Company
Bremerton Freight Car Ferry, Inc.
MTI, Inc.
Washington, Idaho and Montana Railway
Company
MLC Equipment Company
MNT, Inc.